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COMMISSIONER

IN THE MATTER OF THE APPLICATION OF THE
ARIZONA ELECTRIC DIVISION OF CITIZENS
COMMUNICATIONS COMPANY TO CHANGE THE
CURRENT PURCHASED POWER AND FUEL
ADJUSTMENT CLAUSE RATE, TO ESTABLISH A
NEW PURCHASED POWER AND FUEL
ADJUSTMENT CLAUSE BANK, AND TO
REQUEST APPROVED GUIDELINES FOR THE
RECOVERY OF COSTS INCURRED IN
CONNECTION WITH ENERGY RISK
MANAGEMENT INITIATIVES.

Docket No. E-01032C-00-0751

IN THE MATTER OF THE APPLICATION OF
CITIZENS COMMUNICATIONS COMPANY,
ARIZONA GAS DIVISION, FOR A HEARING TO
DETERMINE THE FAIR VALUE OF ITS
PROPERTIES FOR RATEMAKING PURPOSES,
TO FIX A JUST AND REASONABLE RATE OF
RETURN THEREON, AND TO APPROVE RATE
SCHEDULES DESIGNED TO PROVIDE SUCH
RATE OF RETURN.

Docket No. G-01032A-02-0598

IN THE MATTER OF THE JOINT APPLICATION OF
CITIZENS COMMUNICATIONS COMPANY AND
UNISOURCE ENERGY CORPORATION FOR THE
APPROVAL OF THE SALE OF CERTAIN
ELECTRIC UTILITY AND GAS UTILITY ASSETS IN
ARIZONA, THE TRANSFER OF CERTAIN
CERTIFICATES OF CONVENIENCE AND
NECESSITY FROM CITIZENS COMMUNICATIONS
COMPANY TO UNISOURCE ENERGY
CORPORATION, THE APPROVAL OF THE
FINANCING FOR THE TRANSACTIONS AND
OTHER RELATED MATTERS.

Docket Nos. G-01032A-02-0914

E-01933A-02-0914

E-01032C-02-0914

RUCO's CLOSING BRIEF

1 INTRODUCTION

2 The Residential Utility Consumer Office ("RUCO") is not a party to the Settlement
3 Agreement proposed by the Arizona Corporation Commission's ("Commission") Utilities
4 Division ("Staff") and the Joint Applicants. However, RUCO finds much to like about the
5 Settlement Agreement. Unfortunately, even with its favorable resolution of many issues,
6 the Settlement Agreement would result in rate increases of over 20 percent to both the gas
7 and electric customers. RUCO therefore recommends that the Commission modify the
8 Settlement Agreement to provide additional tools for customers to mitigate the rate impacts
9 of the Settlement Agreement.

11 BACKGROUND

12 In September 2000, Citizens Communications Company's ("Citizens") filed an
13 application to recover additional amounts from its Arizona Electric Division customers
14 through its existing purchase power and fuel adjustor clause ("PPFAC") ("PPFAC Case").
15 Citizens amended that application in September 2001, seeking recovery of the balance of
16 the PPFAC account and the costs of its new power supply contract with Pinnacle West
17 Capital Corporation ("Pinnacle West"). In October 2002 Citizens filed an application to
18 increase rates for its Arizona Gas Division ("Gas Rate Case"). The Gas Rate Case sought
19 an increase of almost 29 percent.

20 In December 2002, Citizens, UniSource Energy Corporation ("UniSource"), and
21 UniSource's subsidiary Tucson Electric Power Company ("TEP") (collectively, the "Joint
22 Applicants") filed a joint application for approval of Citizen's sale of its Arizona electric and
23 gas assets to UniSource and approval of related financing transactions ("Joint
24

Application"). In the Joint Application, UniSource indicated that it is willing to forgo the balance of the PPFAC account at the time of closing, which is estimated to be approximately \$135 million, if the PPFAC base rate is adjusted to include full recovery of the costs of power under the new agreement Citizens had negotiated with Pinnacle West. UniSource also indicated that it would attempt to renegotiate the contract with Pinnacle West and share any resulting savings equally with customers, and offered to write down the rate base of the electric assets in the next electric rate case to reflect the price UniSource pays for those assets. UniSource also indicated in the Joint Application that it would seek an increase in the Gas Rate Case of only 23 percent.

The Commission's Utilities Division ("Staff") and the Joint Applicants negotiated a Settlement Agreement to resolve the PPFAC Case, the Gas Rate Case and the Joint Application. Though RUCO could have had concurrent meetings with the Joint Applicants, it was unable to participate in the dynamic "give and take" of negotiations. Tr. at 559-60 (Diaz Cortez).¹ Pursuant to the Settlement Agreement, UniSource would forgo recovery of the PPFAC balance at the time of closing, and the PPFAC base rate would be adjusted to fully recover the costs of the new purchased power contract with Pinnacle West on a going forward basis. As a result of the Settlement Agreement, electric customers would experience an average increase of 22 percent. Exh. RUCO-1 at 3 (Diaz Cortez); Tr. at 535-36 (Diaz Cortez). In addition, UniSource would share any savings resulting from renegotiation of that contract, passing 60 percent of those savings to customers and maintaining 40 percent for itself. UniSource would write down the rate base of the electric

¹ The hearing transcript will be cited herein as Tr. at (pg.#) (Witness). Hearing exhibits will be cited as Exh. __-# at (pg#) (Witness).

1 assets to its purchase price in the next electric rate case. UniSource also agreed to
2 reduce the increase in the Gas Rate Case to 20.9 percent.

3
4 **ADDITIONAL DEMAND SIDE MANAGEMENT TO HELP CUSTOMERS COPE WITH**
5 **RATE IMPACTS OF SETTLEMENT AGREEMENT**

6 While there is much to like in the Settlement Agreement, it would have the
7 unfortunate result of increasing gas customers' rates by almost 21 percent, and electric
8 customers' rates by 22 percent. Tr. at 537 (Diaz Cortez). Though perhaps unavoidable,
9 those increases are substantial. Exh. RUCO-1 at 8 (Diaz Cortez); Tr. at 549 (Diaz Cortez).
10 Therefore, RUCO proposes two modifications to the Settlement Agreement to assist
11 customers in dealing with its rate impacts.²

12 First, RUCO recommends that UniSource increase investment in demand side
13 management ("DSM") programs in the Citizens electric service territories above the current
14 \$175,000 annual expenditure. The increased investment should come in two steps. An
15 incremental \$425,000 of DSM expenditures should be implemented upon the close of the
16 sale. An additional \$400,000 should be contingent on UniSource successfully
17 renegotiating the power supply contract with Pinnacle West. The additional funding should
18 expand Citizens' current DSM programs, and implement several new programs.
19 UniSource should be permitted to defer the costs of the additional DSM programs, with
20

21 ² RUCO finds it necessary to make its recommendations in response to the Settlement Agreement
22 because it was precluded from participating in the negotiation between Staff and the Joint Applicants, and
23 therefore unable to influence the outcome of the Settlement Agreement process. RUCO is not faulting the
24 parties to the Settlement Agreement for the process they undertook. However, the reality is that RUCO was
unable to evaluate the need for its recommended modifications to the Settlement Agreement without
knowing the rate impact of the Settlement Agreement on customers. Tr. at 560, 569 (Diaz Cortez).

1 interest, for future recovery, subject to rapid deployment and successful implementation of
2 the DSM programs. Exh. RUCO-1 at Appendix II.

3 An increase in funding for DSM programs will provide both economic and
4 environmental benefits. Tr. at 577 (Diaz Cortez). RUCO's proposal is driven primarily by
5 the economic benefits customer can experience by decreasing their bills by reducing
6 consumption. *Id.* at 577-78. Fortunately, the Settlement Agreement's increase for electric
7 customers is entirely embedded in the commodity rate. Exh. RUCO-1 at 9 (Diaz Cortez).
8 Therefore, any decrease in consumption will decrease a customer's bill by more than the
9 amount of the rate increase per kwh. In fact, a 19 percent reduction in consumption would
10 hold an average residential customer harmless from the entire increase. *Id.* The
11 additional DSM investment can provide customers with tools to enable them to mitigate
12 some, or all, of the impact of the electric rate increase. Tr. at 537 (Diaz Cortez). Beyond
13 the economic benefits, the environmental benefits of additional and expanded DSM
14 programs are "icing on the cake." Tr. at 577-78 (Diaz Cortez).

15
16 **DECREASE UNISOURCE'S SHARE OF SAVINGS FROM RENEGOTIATION OF**
17 **POWER SUPPLY CONTRACT**

18 RUCO's second proposed modification the Settlement Agreement is an adjustment
19 to the portion of savings that result from any renegotiation of the contract with Pinnacle
20 West that are shared with UniSource. RUCO proposes that, instead of UniSource sharing
21 in 40 percent of any savings, as proposed in the Settlement Agreement, UniSource only be
22 permitted a 10 percent share.

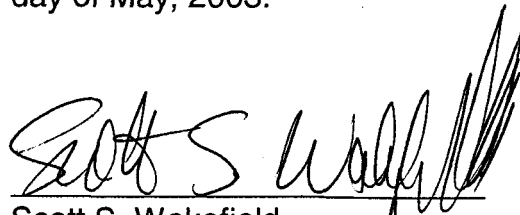
1 Absent the Settlement Agreement, UniSource would not be entitled to any share of
2 savings that result from renegotiating a purchased power contract. Exh. RUCO-1 at 10
3 (Diaz Cortez); Tr. at 329-30 (Jaress). This is because the purchased power adjustor is
4 meant to flow *100 percent* of changes in cost through to customers. Allowing UniSource to
5 keep 40 percent of the savings could result in a windfall to UniSource. If UniSource were
6 able to renegotiate the Pinnacle West contract for a 10 percent reduction, UniSource
7 would realize an additional \$3 million profit *each year*. Exh. RUCO-1 at 10 (Diaz Cortez).
8 Even if UniSource achieves the reduction that Staff witness Lee Smith believes is
9 attainable, UniSource would collect an additional \$600,000 per year as a windfall for
10 merely renegotiating a contract. See Tr. at 332.

11 Though UniSource would generally be entitled to nothing upon renegotiating the
12 power supply contract, RUCO proposes that it be permitted a 10 percent share of any
13 resulting savings. A 10 percent share can provide an effective, yet equitable, incentive for
14 UniSource to negotiate more favorable terms in the power supply contract. Exh. RUCO-1
15 at 10-11 (Diaz Cortez).

16 17 **CONCLUSION**

18 The Settlement Agreement favorably resolves many of the issues raised by the
19 three underlying applications. However, the Settlement Agreement would result in
20 significant rate increases for customers. Therefore, the Commission should modify the
21 Settlement Agreement to provide additional DSM programs, and a more favorable sharing
22 of future power cost savings. These modifications will assist customers in minimizing with
23 the rate impacts of the Settlement Agreement.

1 RESPECTFULLY SUBMITTED this 15th day of May, 2003.

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5 Chief Counsel
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